Mitch on the Markets

Embracing Fear in the Stock Market

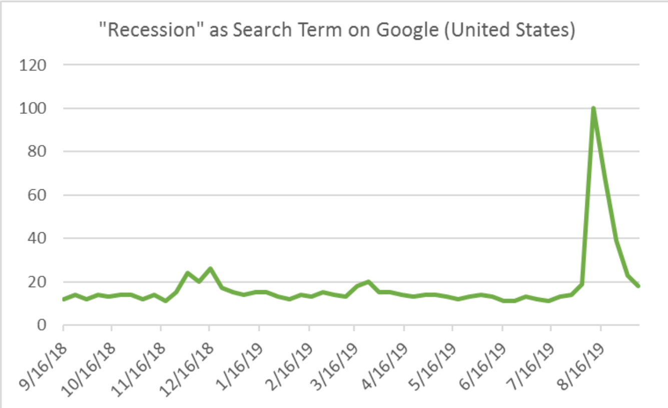
By Mitch Zacks
CEO & Senior Portfolio Manager

Concerns are growing about the strength of the U.S. economy and the longevity of the bull market. You may have noticed that "recession" seems to be the hottest trending topic in the news these days, with any bit of negative data being seized upon as a potential canary in the coal mine. I've even written about the possibility of recession quite a bit in this space in recent weeks, though my commentary tends to illuminate the hard data underscoring modest – but still positive – economic growth.

As fear and concern grow about the fate of the U.S. economy and stocks, my message to you is to look the other way – literally. If you see a scenario where economic data and leading economic indicators point to more growth (check), where governments and central banks are posturing for more stimulus (check), but where fear and negativity are getting worse in the news and amongst investors (check), then in my opinion that's a clear and classic sign that a "wall of worry" is building. And, based on decades of experience in equity investing, I can tell you that markets love to climb a wall of worry.

I'll pull an example from earlier this year to help demonstrate the point. Back in early August, you may remember the sudden and dramatic August 5th decline when the S&P shed 3.3% and the tech-heavy Nasdaq fell -3.8% in a single trading session.[1] In a "Mitch on the Markets" column just a few days after the decline, I asserted my belief that the downside volatility was a correction (and not a bear market), and reminded readers that "*equity market recoveries often happen in "v-shaped" patterns, which means in many cases, the recovery can happen just as quickly as the decline.*" I urged patience in the face of fear.

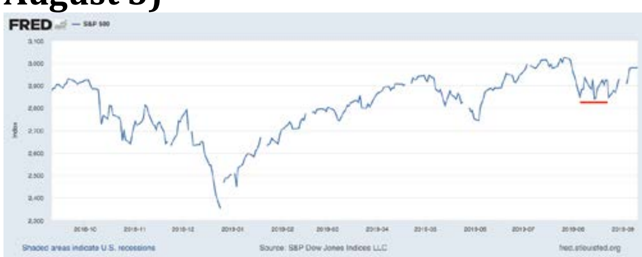
As you can see in the chart below, concern about the U.S. economy bubbled up as a result of the selling pressure. Data from Google Trends shows that searches for recession in the U.S. spiked at precisely the time the S&P 500 entered a volatile patch:



Source: Google Trends[2]

In my experience, it is during these times – when the market goes haywire and investor sentiment shifts decisively to the negative – that bottoming patterns tend to form.

The S&P 500 Over the Last Year (red line indicates 'bottoming' following August 5)



Source: Federal Reserve Bank of St. Louis[3]

For long-term investors who ignore the noise and focus on where the markets will likely be in 10, 20, even 30 years, these events often end up being attractive entry points, in my view. In the example above, the proof is in the pudding: it's only been a little over a month since the big August 5th decline, but the equity markets as measured by the S&P 500 appear to remain in recovery mode. The S&P 500 ended August 5th at 2,844 and is trading today close to 3,015.[4]

Bottom Line for Investors

To be 100% clear, I do not advocate for you to seek out volatility and negative sentiment as a signal to trade in-and-out of the markets. At Zacks Investment Management, we do not believe in short-term market timing. As a client, you already know that we recommend giving yourself the best chance at realizing long-term financial goals by maintaining exposure to risk assets (like stocks) over *long stretches of time,* in the realm of 20+ years.

The point of making "fear your friend" is so that as a savvy and experienced investor, you can see when fear bubbles form in the news – even as the U.S. economy continues to grow and economic data remains solid. When you recognize those disconnects, between *expectations* about future growth and *realities* about future growth, it is easier to resist the urge to make kneejerk reactions to big down days or in response to endless media coverage of recessions and bear markets. We urge you to keep a steady hand, which in my view is the key to long-term investment success.

About Mitch Zacks

Mitch is the CEO & Senior Portfolio Manager at Zacks Investment Management. Mitch has been featured in various business media including the Chicago Tribune and CNBC. He wrote a weekly column for the Chicago Sun-Times and has published two books on quantitative investment strategies. He has a B.A. in Economics from Yale University and an M.B.A in Analytic Finance from the University of Chicago.

[1] Financial Times, September 2019. https://www.ft.com/content/ab8d654c-b71d-11e9-96bd-8e884d3ea203

[2] Google Trend, September 11, 2019. https://trends.google.com/trends/explore?q=recession&geo=US

[3] S&P Dow Jones Indices LLC, S&P 500 [SP500], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/SP500, September 11, 2019.

[4] Yahoo Finance, September 11, 2019. https://finance.yahoo.com/quote/%5EGSPC?p=^GSPC

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